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Restrictive Business Practices

COMPETITION POLICY AND RESTRICTIVE BUSINESS PRACTICES

Issue No. 20

This information note by the UNCTAD secretariat aims to respond briefly to those basic questions which might be posed by government officials, business circles, academics and consumer organizations regarding competition policy, control of restrictive business practices at national and international levels, and UNCTAD's technical assistance programmes in this area.

I. INTRODUCTION

MARKET-ORIENTED REFORMS AND THE NEED FOR COMPETITION

1. Market-oriented reforms have been a matter of concern not only to developed market economies, where the phenomena of deregulation and privatization are commonplace, but also to most developing countries and countries in transition. Most of these countries have undertaken structural adjustment programmes involving far-reaching economic reforms, including price liberalization, which involves gradual (or rapid) scrapping of price-regulations and price-subsidies; demonopolization and privatization of large State-owned enterprises or parastatals; and liberalization of foreign direct investment (FDI) and trade. The latter includes drastic reduction of tariff and non-tariff barriers which previously affected import competition of goods and services.

2. Domestic reforms, such as those listed above, have been strongly enhanced by trade-liberalization agreements at the multilateral level such as the Uruguay Round. As a result, border measures such as tariffs and quotas or non-tariff barriers are being gradually reduced or eliminated, and the traditional distinction between domestic and international markets is becoming

increasingly blurred. Governments, which in the past could shelter domestic producers from foreign competition (usually accused of engaging in "unfair" trade), have less and less scope for using such trade laws to deal with these effects.

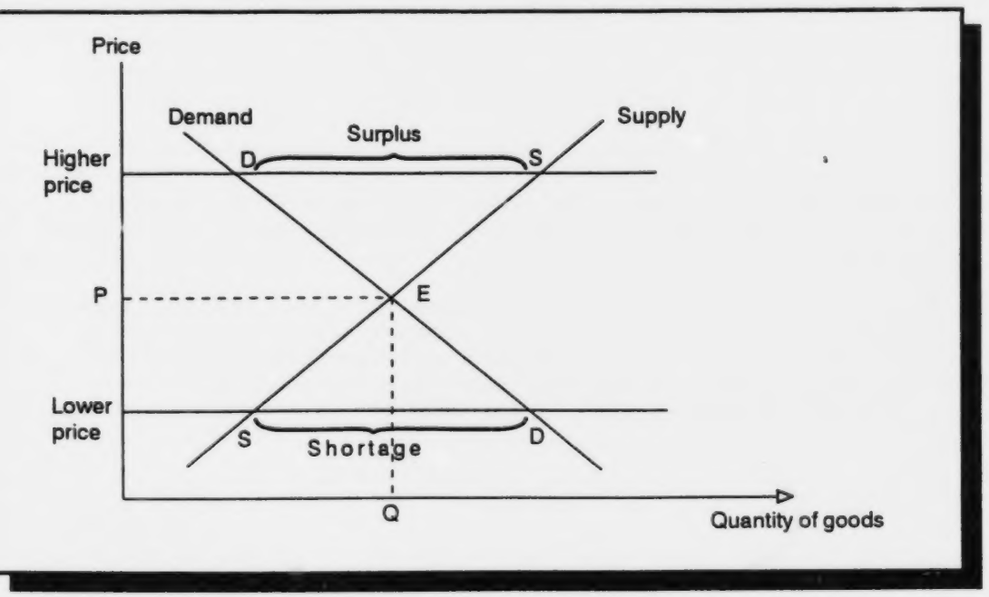
Competition, efficient markets and competitiveness

3. As a result of widespread market-oriented economic reforms mentioned above, a convergence of views is emerging about the positive effects of competition on the efficiency of firms. Competition acts as a powerful incentive for enterprises to respond more rapidly to market signals; to improve the quality of goods and services they provide; to respond better to consumer needs through innovation and R & D, and by supplying quantities commensurate to demand. All this to the benefit of individual consumers, but also of intermediate users such as other providers of goods or services, and hence improves the competitiveness of the economy as a whole.

Competition in place of price regulations

4. Before introducing competition law, many countries used price controls and complex systems of price regulations. Administratively, regulated prices are usually unable to satisfy consumer needs and economic growth at the same time. One of the two objectives has to be sacrificed in favour of the other. For example, if prices are set by administrative regulation, there is little chance that they will correspond exactly to the point of equilibrium where supply and demand curves meet, as can be seen on the chart below.

Chart 1: PRICE EQUILIBRIUM UNDER 'PURE' COMPETITION



5. The upward slope of the demand curve corresponds to the ability and will of firms to supply more quantities when prices are higher. The contrary is true for demand, which will shrink as prices soar. Therefore there is a single point of equilibrium E where both supply and demand meet: this is the price which equates the quantity of goods supplied to that demanded by consumers. When administrative prices are set, the chances are that the Government will fix a price which is either lower or higher than E.

6. If the authorities want to favour specific groups of consumers, they will fix too low prices, which will result in shortages of supply and scarcity, giving rise to long queues in front of shops. Also, as a result of the low price, goods supplied will usually be of poor quality. On the other hand, if the Government wants to set higher than equilibrium (or competitive) prices, for example to protect specific producers (e.g. farmers in the EU), then supply will exceed demand, and the country will be faced with unsold surpluses (e.g. the "mountains" of butter of the European Community). Hence an effective allocation of resources throughout the economy will be achieved by liberalizing prices and letting the market itself set the competitive price.

Optimal allocation of resources, accelerated growth and development

7. As competitive prices are allowed to establish themselves in the economy overall, that economy will achieve optimal allocation of resources, satisfying consumer demand and resulting in the elimination of inefficient structures of production. The elimination of inefficiencies, improvement of quality and incentive for firms to innovate will eventually improve the efficiency of the overall economy, promote growth and, in the final analysis, accelerate development.

Competition and competitiveness in international trade

8. Competitiveness is a concept that should not be confused with competition policy. It is often argued by firms that wish to merge and create large conglomerates at home that, by so restraining competition at home, they will increase their competitiveness in overseas markets. While economies of scale and attainment of "critical mass" or size is an important consideration in achieving worldwide competitiveness, large organizations often also suffer from diseconomies of scale, as well as heavy and bureaucratic structures, and they are unable to adapt rapidly to changing demand and needs of foreign markets. Small and medium-sized firms have often demonstrated much faster adaptability to changing markets and have become highly competitive. Therefore special caution should be given to avoiding State subsidies and distortions to resource allocation in favour of "national champions" which are sometimes inefficient, failing firms. It is often a mistake to believe that shielding firms from competition at home will allow them to win battles abroad. Without the incentives of competition both on the domestic market and abroad, these firms may not achieve the necessary competitiveness. Gradual elimination of State distortions to trade in both domestic and international markets might also be replaced by private restraints to trade and competition, hence the need for competition policy at both national and international (multilateral) levels to ensure that competition is not stifled by restrictive business practices.

II. THE MAIN RESTRICTIVE BUSINESS PRACTICES AND THEIR ADVERSE EFFECTS ON COMPETITION

9. On any given market, enterprises have a natural tendency to compete with each other. The winner makes good profit. The loser makes losses and may be forced out of the market through bankruptcy. New firms may start up and enter the market, and the process continues. Free markets depend on consumer sanctions for firms to enter and - eventually - exit the market place. In the absence of free entry and free exit, competition may easily be stifled.

10. Under the incentive of competition, firms will be obliged to perform the best they can, in order to satisfy consumer needs. They will constantly try to guess those needs of the consumer through R & D and innovation. However, the preferred situation for any supplier on any market is to have a monopoly.

Monopolies and dominant firms

11. A monopoly can exist for a number of reasons. There are "natural" monopolies for reasons of economies of scale, for example when the size of the market does not allow the existence of more than one electric power plant, or when it does not make sense to have two parallel telephone lines or water distribution systems.

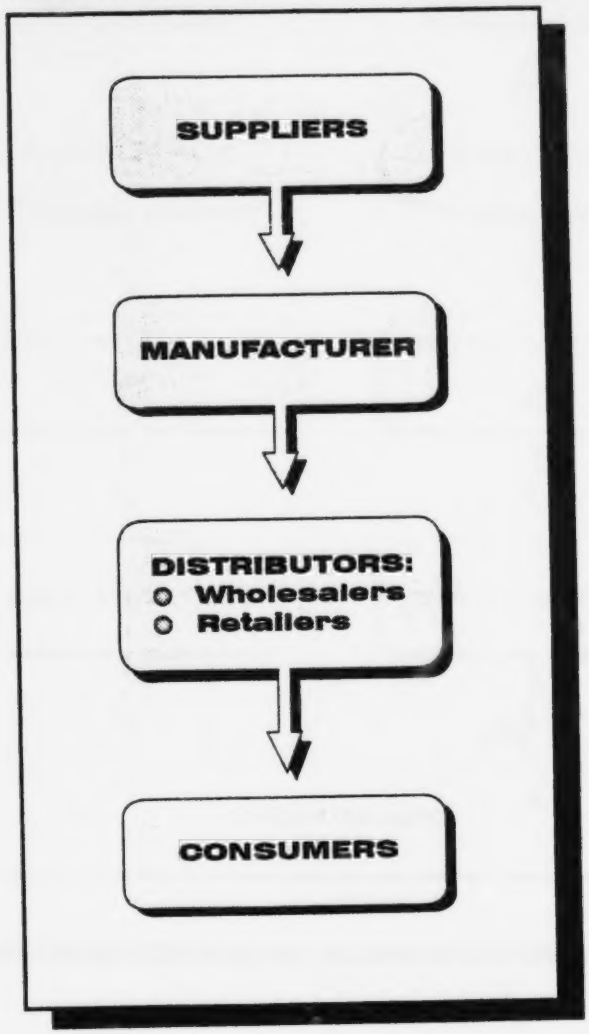
12. Monopolies are often attributed by State regulation. In other cases, for safety or many other reasons, the State may regulate the number of firms authorized to operate on a given market. Airlines may be tightly controlled for safety or banks may be chartered for prudential reasons, to ensure that those authorized will not fail. By so doing, however, the State reduces or eliminates competition, and at times it has done so in sectors such as hairdressers and tobacconists, where there was no evident justification on grounds of safety or otherwise.

13. Firms may also be tempted to reduce or eliminate competition without State interference because a monopolist can maximize profit. Actions by firms aimed at reducing or eliminating competition are called restrictive business practices (RBPs). 1/ If they eliminate all competition, they become a monopolist. If they reduce competition substantially, to a degree where existing competitors will not try to challenge their price decisions, they create for themselves a so-called "dominant position of market power" (DPMP). Like monopolists, dominant firms are able to set high prices without being affected by competitors, even though there are other firms in the market. To be able to do this, a dominant firm will usually be consistently larger or have "deeper pockets" than its competitors, the latter accepting to adapt their prices to those set by the dominant firm - i.e. to "follow the leader". 2/ An enterprise can gain a monopoly position by legal means: through innovation and/or diversification of its products, both of which are protected by intellectual property rules. But it can also do it by using restrictive business practices.

14. Two main types of RBPs exist. They are often referred to as horizontal or vertical practices.

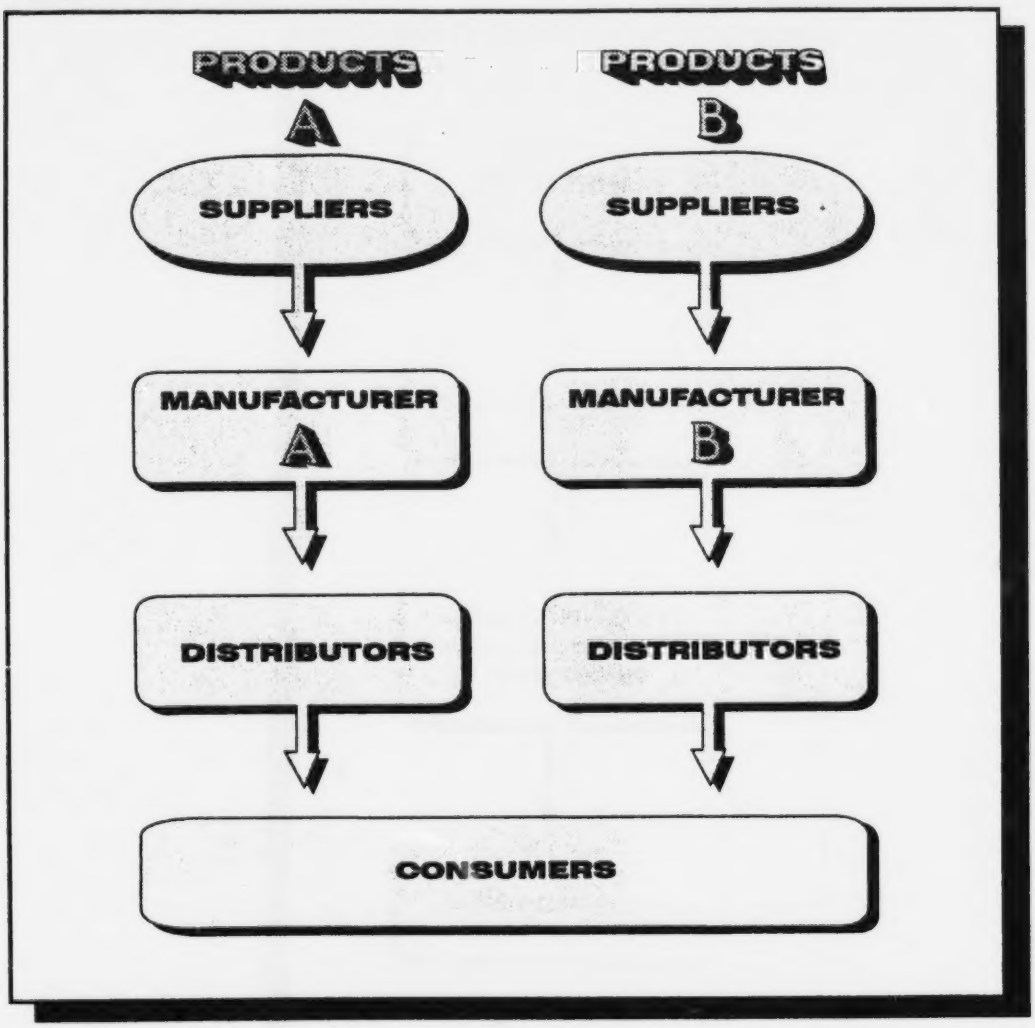
15. The terminology of "horizontal" or "vertical" RBP refers to the production-distribution chain, which is usually described by a chart representing the vertical flow of goods, from suppliers of raw materials to the manufacturer, his distributors and finally, the consumer, as described below.

Chart 2:
PRODUCTION-DISTRIBUTION CHAIN



In the case of two (or more) firms competing to supply identical or similar goods, there are two (or more) similar vertical production- distribution chains, as follows:

Chart 3:
PRODUCTION-DISTRIBUTION CHAIN OF TWO COMPETITORS: FIRM A AND FIRM B



In case of a cartel, there is a horizontal agreement between manufacturers A and B. But cartels can be at the level of suppliers, distributors (horizontal), or even among different members of the chain, in which case the agreement is both horizontal and vertical. In the case of a single firm (monopolist or a dominant firm), it will be able to use its market power to impose a series of restraints on his distributors (downstream) or its suppliers (upstream). This is why the RBPs used by the firm over its suppliers or distributors are called "vertical RBPs".

A. Horizontal RBPs or cartel agreements

16. In the first case, there are many firms supplying a given market (e.g. automobile firms selling similar types of vehicles). Instead of competing, auto manufacturers might decide to fix the prices which assure them the highest profits, in the same way as if they were in a monopoly. Such an agreement is called a cartel. The only difference from a monopoly is that members of the cartel will have to agree to share the market among themselves, so that each new "monopolist" has his guaranteed market share. They will also try to eliminate outsiders to the agreement, as new entrants to the market might be tempted to cut prices and thus ruin the advantages provided to its members by the cartel. To avoid this inconvenience, cartels usually establish so-called "combat funds" which enable them to force outsiders either to join the cartel, or to be eliminated by systematically underbidding their offers to customers. For example, firms were found to have preferred to "offer" their goods or services for a symbolic sum of one dollar, in order to ensure that their competitors were kept outside of their "preserved market".

17. There are four main types of cartels:

(a) Domestic cartels. An example of such a cartel would be one regulating the production, distribution and after-sales network of bicycles. If such a cartel covers a large enough share of the market (say 90 per cent of manufacturers and distributors), then it becomes very difficult for outsider manufacturers of bicycles to sell into that market (since no dealer member of the cartel will agree to sell their product unless they also join the cartel). Strong domestic cartels can therefore seriously hamper imports. In fact, they are often supplemented by an import cartel as well;

(b) Import cartels. These cartels often act as centralized buying organizations for the supply of raw material inputs to an industry, for example chemicals. They can be established to countervail the market power of export cartels in other countries;

(c) Export cartels. In almost all countries having RBP legislation, the law either specifically exempts such cartels provided they are notified, or it simply does not cover such cartels as a result of the "effects principle", i.e. where the effects are not felt in the domestic market the law does not cover such arrangements;

(d) International cartels. When enterprises in different countries join to fix prices, allocate markets (share markets), or take turns in projects being awarded to them, one speaks of an international cartel.

Characteristics of cartels

Restrictive practice	Type of action
Price fixing	Uniform sales conditions
	Collusive tendering (bid-rigging)
Market allocation	Geographical allocation
	Customer allocation
	Taking turns in projects
Elimination of outsiders	"Combat funds" and predatory pricing to under-bid non members

18. In all these forms of cartels, there is the possibility of collusive tendering, i.e. where the members of the cartel take part in tenders and submit what is called "cover bids" in order to ensure that the cartel member whose turn it is to be awarded the contract effectively submits the most attractive bid and is thus selected. Of course, even the winner will have offered an exaggerated cartel price for the project in question.

B. Vertical restrictive business practices

19. A monopoly or a dominant firm can make use of RBPs to take unfair advantage of its strong market power over its suppliers or distributors. There are numerous vertical RBPs, among which:

(a) Resale price maintenance, whereby the manufacturer fixes the price at which he obliges the distributor to sell; the latter is impeded from fixing his own margin. If he discounts the goods in question, the manufacturer will refuse to continue to supply him;

(b) Refusal to deal, in which case the distributor will be in trouble, since he has lost his source of supply and will have difficulty to find a replacement, as the supplier is a dominant firm. (In the case of a monopolist, the distributor has no chance of finding a replacement.) By threatening to stop supplying his distributors, a monopolist or a dominant manufacturer can force them to accept a whole range of vertical RBPs, including resale price maintenance and the practices listed below;

(c) Exclusive dealing, which involves an undertaking by the manufacturer that he will give exclusive supply to the dealer in a given market (for example, a city, a region, or a country), thus guaranteeing him a monopoly in that market. It is important to note that exclusive dealing is a customary business arrangement which is usually pro-competitive. It allows the manufacturer to ensure that his distributor will maintain necessary quality and after-sales service. However, in the case of exclusivity granted by a monopolist or a dominant firm, anti-competitive effects can occur. In

particular, to maintain the monopoly position of his exclusive dealer (or agent) in a given market, the manufacturer may attempt to block parallel imports (e.g. imports by independent dealers who import the same goods from cheaper sources abroad);

(d) Reciprocal exclusivity, which implies that the distributor undertakes to sell exclusively the goods of his exclusive supplier and no-one else's;

(e) Differential pricing, which involves the maintenance of different prices in different markets in order to extract the maximum prices which different types of consumers can afford. This practice can occur when a manufacturer wants to fix different prices in different countries, and tries therefore to block parallel imports;

(f) Tied selling, whereby the manufacturer forces the resaler or wholesaler to hold more goods than he wishes or needs. In other cases, the purchaser is forced to take more products than he wants (e.g. if he needs a computer, he is forced to buy the software as well; if he wants spare parts, he has to buy large quantities of them). The distributor may be forced to hold the whole range of the manufacturer's products: this RBP is called full-line forcing. A dominant firm may abuse its power to force the sale of other, non-needed goods with those for which it has a monopoly or a dominant position.

(g) Predatory pricing, where the supplier sells at a very low price (often below cost) in order to drive his competitors out of business, or he supplies intermediate inputs to competitors at excessive prices, with the same goal in mind. (It should be noted that this will be possible only if the supplier is a dominant firm, since otherwise, the competitor will have no difficulty to find a replacement at a market price.);

(h) Transfer pricing, which involves over-invoicing or under-invoicing intermediate inputs between a parent and a subsidiary enterprise. In the case of over-invoicing, the subsidiary (in another country) can declare less profits and thus evade taxes or circumvent profit-remittance restrictions. Strictly speaking, this is not an RBP. However, under-invoicing can be used as a method of predatory (lower) pricing in order to drive competitors out of business with the aim of creating a monopoly.

C. Mergers and acquisitions

20. Concentration of market power through mergers, takeovers or joint ventures constitutes yet another type of restrictive business practice when they are used to create a monopoly or a dominant position of market power in a given market. A merger or takeover of two competing firms may create similar results to those of a cartel agreement.

III. ACTION AT NATIONAL AND INTERNATIONAL LEVELS: THE SET OF PRINCIPLES AND RULES

A. Action at national level

21. While all Governments are aware that certain business practices have adverse effects on their country's interests, officials are not always sensitized to the existence of specific RBPs, and the official bodies tackling issues where RBPs could be discovered are often dispersed in different Ministries and administrations (e.g. the Central Bank, the Customs Administration, the Ministries of Foreign Trade or of Industry, etc.), each one dealing with diverse issues such as direct foreign investment, transfer of technology, programming and planning of domestic industry, government procurement, import licensing and export promotion. In such circumstances, effective action in detecting and tackling specific cases of RBPs may not be taken because of the absence of a conscious competition policy and procedures aimed at controlling and eliminating RBPs. The elaboration of precise criteria for the detection of RBPs in the sectors where they occur is therefore essential if effective action to tackle RBPs is to be taken.

22. The only way to control effectively RBPs that have adverse effects is to enforce national competition legislation strictly. To date, all developed countries as well as economies in transition have adopted, or are in the process of adopting, competition legislation. 3/ With increased liberalization and globalization of international markets, however, national competition laws are sometimes unable to control effectively anti-competitive practices which affect the domestic market, but originate from abroad. In other cases, fact-finding might have to be undertaken abroad, encroaching over the sovereignty of other nations. Differences in degrees of application of national competition laws may result in trade disputes among trading partners. For many such reasons, international consensus on the main principles of competition, leading to increased "common ground" on rules and cooperation in the control of restrictive business practices, is a necessity.

B. Action at international level: the Set of Principles and Rules for the Control of Restrictive Business Practices

23. Proposals to control RBPs by private enterprises were already included in Chapter V of The Havana Charter in 1946, and in GATT negotiations in the 1960s. All those attempts were inconclusive. In 1980, however, after almost 10 years of negotiations between developed, developing and centrally-planned economies, agreement was reached in UNCTAD on a voluntary code of conduct on competition: the Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices. 4/

The Set of Principles and Rules for the Control of RBPs

Objectives

24. The Set's first objective is to ensure that RBPs do not impede or negate the realization of benefits that should arise from the liberalization of tariff and non-tariff barriers affecting world trade, particularly those affecting the trade and development of developing countries. It also seeks to

attain greater efficiency in international trade and development through, inter alia, promoting competition, control of concentration of economic power and encouragement of innovation. Moreover, it aims at protecting and promoting social welfare in general and, in particular, the interests of consumers.

Voluntary nature of the Set

25. The Set, as adopted by the General Assembly in its resolution 35/63 of 5 December 1980, is in the form of a recommendation. In other words, its application and implementation depends upon the willingness of States which have accepted the Set to meet their commitment to it. Moreover, it is stipulated in the Set that, in the performance of its functions, neither the Intergovernmental Group of Experts on Restrictive Business Practices, established in UNCTAD to provide the institutional machinery for the Set, nor its subsidiary organs "shall act like a tribunal or otherwise pass judgement on the activities or conduct of individual Governments or of individual enterprises in connection with a specific business transaction". It is also stipulated in section B (ii) of the Set, "Scope of application", that the Set "shall not apply to intergovernmental agreements, nor to RBPs directly caused by such agreements".

The scope of the Set

26. The Set applies to all enterprises, including transnational corporations, whether private or State-owned, and it is universally applicable to all countries and to all transactions in goods and services. It also applies to regional groupings of States (such as the European Union and the European Economic Area), to the extent that they have competence in the area of competition law and policy.

Preferential or differential treatment for developing countries

27. Under section C of the Set, which lists multilaterally agreed principles for the control of RBPs, the specific needs of developing countries, and in particular the least developed, are taken into account, as it was agreed that "in order to ensure the equitable application of the Set of Principles and Rules, States, particularly developed countries, should take into account in their control of restrictive business practices the development, financial and trade needs of developing countries, in particular of the least developed countries, for the purposes especially of developing countries in:

> "(a) Promoting the establishment or development of domestic industries and the economic development of other sectors in the economy, and
>
> "(b) Encouraging their economic development through regional or global arrangements among developing countries."

The Set and enterprise behaviour, including transnational or multinational corporations: prohibited horizontal and vertical practices

28. Section D of the Set states that "enterprises should conform to the restrictive business practices laws and the provisions concerning restrictive

business practices in the laws of the countries in which they operate and, in the event of proceedings under these laws, should be subject to the competence of the courts and relevant administrative bodies therein". Paragraphs 3 and 4 of section D deal with the main types of RBPs that enterprises should refrain from. Concerning intra-firm transactions between different entities of a transnational corporation, while paragraph 3 excludes enterprises "when dealing with each other in the context of an economic entity wherein they are under common control, including through ownership, or otherwise not able to act independently of each other", paragraph 4 covers all enterprises which "limit access to markets or otherwise unduly restrain competition ... through an abuse or acquisition and abuse of a dominant position of market power". This same paragraph goes on to list practices in this respect, which include predatory behaviour towards competitors and "discriminatory (i.e. unjustifiably differentiated) pricing or terms or conditions in the supply or purchase of goods or services, including by means of the use of pricing policies in transactions between affiliated enterprises which overcharge or undercharge for goods or services purchased or supplied as compared with prices for similar or comparable transactions outside the affiliated enterprises".

Action by States at national, regional and subregional levels: competition legislation and cooperation between national competition authorities

29. In order for States to be able to take effective action against RBPs, the Set calls for the adoption, improvement and effective enforcement of appropriate legislation and the implementation of judicial and administrative procedures. In this respect, continued work is also prescribed within UNCTAD on the elaboration of a model law or laws on RBPs in order to assist developing countries in devising appropriate legislation. UNCTAD and other relevant organizations of the United Nations system working in conjunction with UNCTAD are also to provide technical assistance, and advisory and training programmes for this purpose.

30. In order to facilitate the control of RBPs by States, the Set calls for the institution of improved procedures for obtaining information from enterprises, including transnational corporations, and the establishment of appropriate mechanisms at the regional and subregional levels to promote exchange of information on RBPs and to assist each other in this area.

Action at the international level

31. This includes in particular the establishment of consultation procedures whereby a State may request a consultation with other States in regard to issues concerning the control of RBPs. In this connection, the States involved may request the Secretary-General of UNCTAD to provide mutually agreed conference facilities for such consultations. Action at the international level at UNCTAD also includes work by the Intergovernmental Group of Experts on Restrictive Business Practices and the United Nations Conferences to Review All Aspects of the Set (the Review Conferences).

C. The Intergovernmental Group of Experts and Review Conferences

32. The Intergovernmental Group of Experts on Restrictive Business Practices, established in 1981, provides a forum for multilateral consultations, discussions and exchange of views between States on matters related to the Set and undertakes and disseminates periodically studies and research on RBPs. It also monitors UNCTAD's technical cooperation activities in the area of competition law and policy.

33. The First Review Conference, which was convened by the General Assembly five years after adoption of the Set, in 1985, was followed by the Second and Third Review Conferences, respectively in 1990 and November 1995.

34. The Third Review Conference (13-21 November 1995) adopted a resolution 5/, in which it established a comprehensive work programme for UNCTAD in the field of competition law and policy, affirmed the fundamental role of competition law and policy for sound economic development and recommended the continuation of the "important and useful work programme within UNCTAD's intergovernmental machinery that addresses competition law and policy issues, and proceeds with the active support and participation of competition law and policy authorities of member countries" (para. 13 of the resolution). It further recommended to the General Assembly to change the name of the Intergovernmental Group of Experts on Restrictive Business Practices to that of Intergovernmental Group of Experts on Competition Law and Policy and to convene a Fourth Review Conference in the year 2000.

IV. TECHNICAL COOPERATION ON COMPETITION LAW AND POLICY

35. In line with provisions 6 and 7 of section F of the Set, and the resolutions adopted by the Second and Third Review Conferences, UNCTAD provides technical assistance and advisory and training programmes on competition law and policy to developing countries and countries in transition. Given the considerable interest in developing and other countries for the adoption of competition legislation, UNCTAD receives a constant flow of requests for technical assistance in this field, which can only be attended to when financial resources are made available.

A. The main types of technical cooperation by UNCTAD

36. The main types of requests so far are as follows:

(a) States without any competition legislation may request information about restrictive business practices, their existence and possible adverse effects on their economy. This may involve a study of the restrictive business practices in their economy;

(b) States without legislation in this field may request introductory seminars directed at an audience which would include government officials and academics, as well as business and consumer-oriented circles;

(c) States which are in the process of drafting competition legislation may request information on such legislation in other countries, and seek advice as to drafting their competition legislation;

(d) States which have just adopted competition legislation may seek appropriate advice for the setting-up of the competition authority; this usually includes training of officials responsible for the actual control of RBPs, and may involve training workshops and/or on-the-job training with competition authorities in countries having experience in the field of competition;

(e) States which have already adopted such legislation and have experience in the control of RBPs may wish to consult each other on specific cases and exchange information; seminars may be organized for such exchanges between competition authorities;

(f) States which wish to revise their competition legislation might seek expert advice from competition authorities in other States, so as to amend their laws in the most effective manner possible;

(g) In addition, a number of countries, such as Germany, Sweden and the United Kingdom, have accepted UNCTAD requests to train foreign competition officials at the premises of their competition authorities. Such exchanges of personnel, although time-consuming and difficult to organize - sometimes for language or confidentiality reasons - might be one of the most effective ways of on-the-job training for officials of recently established competition authorities.

B. How to request and obtain assistance from UNCTAD

37. A formal request should be addressed to the Secretary-General of UNCTAD, indicating the types of RBP assistance and/or advisory mission which is envisaged.

38. For national assistance services, the possibilities of UNDP/IPF assistance should be explored with local UNDP services before addressing UNCTAD's RBP Trust Fund (INT/86/A01).

Notes

1/ It should be noted that terminology in this area is very rich (and confusing), as some countries refer to restrictive trade practices to mean the same thing.

2/ For more detailed tests to determine the existence of DPMP, see chapter II of TD/B/RBP/INF.37 on Competition Policy and Competition Legislation.

3/ For a detailed examination of recent trends and characteristics of competition legislation, see UNCTAD, "Competition Policy and Competition Legislation: Information Issue No. 21 (TD/B/RBP/INF.37).

4/ The Set is contained in doc. TD/RBP/CONF.10/Rev.1.

ANNEX

Main technical assistance activities of UNCTAD in the area of competition (1986-1995)

Year	Type of activity	Country(ies) of participants	Foreign experts from:	Location
1986	Regional seminar for Africa	Botswana Egypt Ethiopia Gambia Ghana Kenya Lesotho Liberia Somalia Swaziland United Republic of Tanzania Zambia Zimbabwe	Federal Republic of Germany Norway Sweden	Nairobi (Kenya)
1987	Regional seminar for Asia	Bangladesh Brunei Darussalam Myanmar China Democratic People's Republic of Korea Fiji India Islamic Republic of Iran Nepal Papua New Guinea Philippines Republic of Korea Sri Lanka Thailand Viet Nam	Federal Republic of Germany Japan Norway Sweden	Bangkok (Thailand)
1988	None			

Year	Type of activity	Country(ies) of participants	Foreign experts from:	Location
1989	Regional seminar for Africa	Angola Benin Burkina Faso Burundi Cameroon Cape Verde Central African Republic Chad Comoros Congo Côte d'Ivoire Djibouti Equatorial Guinea Guinea Madagascar Mali Morocco Mozambique Niger Rwanda Sao Tome and Principe Senegal Togo Tunisia Zaire	France Spain EEC	Douala (Cameroon)
1990 September	Regional seminar for Latin America	Bolivia Brazil Chile Cuba Ecuador El Salvador Guatemala Honduras Mexico Nicaragua Paraguay Peru Trinidad and Tobago Uruguay Venezuela	Federal Republic of Germany Norway Sweden United States of America	Caracas (Venezuela)
	National seminar	Cuba	Sweden	Havana (Cuba)
1991 February	National seminar	Ghana	Germany	Accra (Ghana)
March	National seminar	Zambia	Netherlands	Lusaka (Zambia)
June	National seminar	Indonesia	Netherlands Sweden	Djakarta (Indonesia)

Year	Type of activity	Country(ies) of participants	Foreign experts from:	Location
1991 (cont'd) September	Subregional symposium on competition	Bangladesh China Fiji Islamic Republic of Iran Myanmar Philippines Republic of Korea Sri Lanka Viet Nam	United States of America Philippines	Seoul (Republic of Korea)
	Subregional seminar/exchange of experience	India Sri Lanka Thailand	Germany	Bangkok (Thailand)
November	Subregional workshop for ASEAN countries	Brunei Darussalam Indonesia Philippines Thailand	Netherlands Norway	Manila (Philippines)
1992 March	Advisory mission	Colombia		Bogotá (Colombia)
	Advisory mission	Trinidad and Tobago		Bogotá (Colombia)
	Advisory services on drafting legislation	Ghana	Germany United Kingdom	Accra (Ghana)
September	National seminar	China	France Norway United Kingdom	Beijing (China)
	National seminar	Viet Nam	France EEC	Hanoi (Viet Nam)
October	National seminar	Argentina	Germany	Buenos Aires (Argentina)
1993 February	National seminar (exchange of experience)	India	Germany	New Delhi (India)
March	Subregional seminar	El Salvador Guatemala Honduras	Norway Sweden	Guatemala City (Guatemala)
	Subregional seminar	Costa Rica Nicaragua Panama	Norway Sweden	Panama City (Panama)

Year	Type of activity	Country(ies) of participants	Foreign experts from:	Location
1993 March (cont'd)	Regional seminar for CARICOM	Antigua and Barbuda Bahamas Barbados Dominica Grenada Guyana Jamaica Montserrat	Canada Norway Sweden	Bridgetown (Barbados)
June	National seminar	Egypt	Germany	Cairo (Egypt)
1994 January	National seminar	Malaysia	Australia Norway Pakistan	Kuala Lumpur (Malaysia)
February	Regional seminar for FORUM countries	Cook Islands Fiji Kiribati Papua New Guinea Solomon Islands Tonga Samoa	Australia Norway New Zealand	Suva (Fiji)
March	National seminar	China	Germany United Kingdom	Shanghai Shenzhen (China)
June	World Bank/UNCTAD Conference on Competition Policy and International Trade	Chile Colombia Peru Venezuela Mexico	United States of America EU	Bogotá (Colombia)
	Subregional seminar	Bahamas Belize Jamaica	Norway	Kingston (Jamaica)
	National seminar	Trinidad and Tobago	Jamaica Norway	Port of Spain (Trinidad and Tobago)
August	National seminar	Philippines	Germany	Manila (Philippines)
December	National seminar	Dominican Republic	Norway Venezuela	Santo Domingo (Dominican Republic)
	National seminar	Costa Rica	Norway Venezuela	San José (Costa Rica)
	National seminar	Nicaragua	Norway	Managua (Nicaragua)
	National seminar	El Salvador	Norway	San Salvador (El Salvador)

Year	Type of activity	Country(ies) of participants	Foreign experts from:	Location
1994 December (cont'd)	National seminar	Peru	Germany	Lima (Peru)
1995 January	International/ CUTS Conference	India	Germany Pakistan Philippines Republic of Korea	New Delhi (India)
February	National seminar	Guatemala		Guatemala City (Guatemala)
	Advisory mission	El Salvador		San Salvador (El Salvador)
October	Regional African seminar	Tunisia Morocco Egypt South Africa Gabon Mauritania Kenya Zambia Zimbabwe	France World Bank	Tunis (Tunisia)
	Regional seminar for Latin America and the Caribbean	Argentina Bolivia Brazil Chile Peru Colombia Venezuela Jamaica Dominican Republic Trinidad and Tobago Mexico Guatemala El Salvador Panama Costa Rica Nicaragua	World Bank	Caracas (Venezuela)
	National seminar	Bolivia	Germany	La Paz (Bolivia)
December	National seminar	Zambia	Kenya Norway Pakistan South Africa United Kingdom	Lusaka (Zambia)
	Advisory mission	South Africa	Norway United Kingdom	Pretoria (South Africa)
	National seminar	Pakistan	Germany	Islamabad (Pakistan)

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COMPETITION POLICY AND LEGISLATION

Information Issue No. 21

This note by the UNCTAD secretariat attempts to clarify legal issues related to competition policy and summarize the basic characteristics of competition legislation.

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Introduction

THE NEED FOR COMPETITION POLICY AND COMPETITION LEGISLATION

Competition policy and competitiveness

1. Competition policy has a wider connotation than competition legislation, the latter being a means to the end of competition policy. Another difference of terminology relates to competition versus competitiveness. It is sometimes argued that competitive economies do not need competition policy or competition legislation. In countries undertaking market-oriented reforms, for example, it was initially believed that opening the domestic market to import competition would be sufficient to create competitive markets without distortion. Some countries with highly successful sectors geared to compete in international markets have not felt the need to adopt competition legislation to ensure competitiveness on international markets; instead, they have dealt with particular anti-competitive practices by regulating specific sectors and certain activities such as government procurement (to avoid collusive tendering). However, under the pressure of market liberalization and globalization, it is generally admitted by a rapidly growing number of countries that competition policy, and hence competition legislation, is an essential element of the competitiveness of nations. This is also widely recognized in the United Nations Set of Principles and Rules for the Control of Restrictive Business Practices, 1/ adopted in 1980 by the United Nations General Assembly.

Competition policy and competition law

2. It has also been argued that, given the cost of introducing competition control mechanisms (legislation and Competition Authority), as well as the difficulties in implementing such complex concepts correctly, it may be preferable to avoid controls altogether and to let market forces, in the long run, resolve temporary restraints to competition. Moreover, sceptics of competition policy in developed countries have also argued at times that such complex concepts are even more hazardous if introduced in developing countries or in least developed countries. It should be noted, however, that competition policy without effective competition law is like an automobile without an engine. Even if implementation is gradual in the first years of application of a competition law, there is an essential learning process that needs some time to develop. For many developing countries and former centrally planned economies, the concepts of competition are very new. There is need for time and training to change mentalities and to create a "culture of competition". The first steps of newly established competition authorities, therefore, are often essentially educational with respect to business and consumer behaviour.

3. Moreover, the legislative process itself is an evolutionary one. Even developed countries have amended and improved their competition laws periodically. Developing countries need to go through a similar "learning process". But if market-oriented economic reforms are to be given a chance to succeed, there is need for competition policy, and such a policy needs competition legislation and a competition authority to monitor its application.

Competition law and economies of scale

4. Market size and economies of scale might require the existence of a single firm in a given situation. However, with respect to tradable goods and services, market liberalization and technological change might remove the justification for the existence of most monopolies, or cause the "relevant market" to switch from the domestic market to the world market, hence transforming a national monopoly into a single national supplier in the world market, with the monopoly situation having disappeared as a result of trade liberalization.

Competition law and foreign investment

5. It is also sometimes argued that competition legislation might deter foreign investment. However, serious implementation of competition policies and effective competition legislation applied in a fair and non-discriminatory manner will, on the contrary, reassure foreign firms that they will be treated in the same way as in their home market and that they will not face restrictive business practices from local competitors, private or public.

6. A number of arguments often put forward against the adoption of competition legislation are listed in annex 1 to this note. Annex 2 sets out some of the difficulties and limitations often encountered by competition authorities once they have been established. Irrespective of such arguments and difficulties, the present information note aims at clarifying legal issues related to competition policy with a view to convincing the reader of the need for all countries to adopt competition legislation in implementation of a competition policy. While chapter I aims at clarifying the links of competition law with various other laws and concepts, such as foreign direct investment, unfair trade, intellectual property rules, consumer protection, etc., chapter II sets out in detail the basic structure and contents of any competition law, and chapter III describes in as pragmatic a manner as possible basic procedures for investigating restrictive business practices or controlling mergers.

Chapter I

COMPETITION LAW AND RELATED LAWS AND CONCEPTS

7. Competition legislation is related in one way or another to a number of other laws and concepts, such as trade laws, FDI rules and intellectual property rules. Consumer protection rules, unfair competition, unfair trading and misleading advertising laws and price regulations may also have goals or provisions in common with or similar to those of competition law. However, a great deal of confusion can develop as a result of vague knowledge of often confusing terminology. Countries having no specific competition law might to a certain extent try to rely on such related bodies of law which cover some aspects of competition law but at the same time have fundamental differences.

A. Consumer protection

8. Many developing countries adopt consumer protection legislation before, or at the same time as, competition legislation. As their name indicates, the objective of such laws is to protect the safety, health and economic interest of consumers, while competition law is directly aimed at promoting competition and efficiency in the economy and only indirectly defends the economic interests of consumers. As can be seen in chart I, however, competition law sometimes includes specific consumer protection provisions, such as prohibition of unfair trade practices (India) and obligation in respect of price labelling (France).

B. Price regulations

9. Some national laws contain provisions related to RBPs and price regulation. As a result of economic reforms and price liberalization, many countries have gradually eliminated administrative regulation of prices and replaced this system by modern competition law (e.g. Norway, Sweden, France, Thailand), though some competition laws still provide the possibility of enforcing price regulations in case of emergency (e.g. France). Moreover, all competition laws prohibit the practices of resale price maintenance (RPM) or price-fixing.

C. Intellectual property rights (IPRs)

10. IPRs, including patents, copyrights, industrial designs and trade marks, in fact provide a monopoly to the owner (inventor or buyer) of an IPR. At first sight, such laws appear to be in direct contradiction with competition laws, which combat monopolies. However, deeper analysis comes to the conclusion that lack of IPRs would discourage investments in R & D and reduce innovation, which is one of the main benefits deriving from competition. Hence the need for IPRs, which in effect are deemed to be pro-competitive overall, since firms that can enjoy such protection will be encouraged to compete by investing in R & D. Restraints, including major RBPs, can, however, be imposed through the licensing procedure of an IPR. Trade marks can be used to seal off and monopolize specific markets. Views differ as to where the borderline lies between intellectual property rights which are pro-competitive and rights which are abusive and anti-competitive. Views on this borderline between competition law and IPRs need to be studied further.

D. Trade laws

11. Trade laws in general are closely related to competition laws, since they have important effects on competition. In principle, dumping, which is the equivalent in international trade of predatory pricing, can justifiably be banned as being anti-competitive. However, anti-dumping rules might, in their application, have important anti-competitive side-effects. For example, anti-dumping action in some cases might close local markets to outside competition and reinforce local dominance by a few firms or by a cartel. Subsidies may distort competition, and countervailing duties can also have anti-competitive spill-over effects. Both dumping and subsidies are usually considered "unfair trade" practices. Safeguards may also result in closing markets to import competition. On the other hand, competition law prohibits (or exempts) import and export cartels which have direct effects on trade. One could also imagine a discriminatory application of competition law which could result in a certain degree of protectionism and adverse effects on trade.

E. Foreign direct investment (FDI)

12. Competition and FDI rules are related on more than one count. First, restrictive FDI rules, imposing, for example, local content requirements or minimum export requirements, as existed until most of these rules were liberalized at the end of the 1980s, were used as a means to regulate the conduct of TNCs operating in a country through the establishment of a subsidiary.

13. Moreover, FDI rules allowing tax holidays, special conditions for imports of inputs, etc. create anti-competitive conditions for the local firms which do not benefit from such facilities.

14. Thirdly, mergers and acquisitions of local firms by foreign entities may create monopoly situations or dominant firms. Especially in countries where FDI restrictions have been relaxed, competition rules, applied in a perfectly non-discriminatory fashion, may still be the best means of getting to grips with possible adverse effects of FDI.

15. Finally, as indicated earlier, competition legislation is applied to all firms operating on national territory, hence to subsidiaries of foreign firms. This should avoid foreign firms from being boycotted by local cartels or restrictive vertical agreements and, conversely, it should ensure that foreign firms do not bring with them habits of collusive tendering and other restraints on trade, including abuse of dominant position of market power.

F. Misleading advertising

16. Some countries have specific marketing laws, and others adopt laws against misleading advertising, which is both a consumer-protection measure and also a pro-competitive provision, since business can compete "unfairly" by publishing misleading allegations and advertisements.

G. Unfair competition

17. The concept of unfair competition (concurrence déloyale in French or competencia desleal in Spanish) is a misleading one, as it is easily confused with competition (anti-trust) law but in reality covers many other concepts, including metrology (weights and measures), misleading representations and advertising, as well as counterfeiting of trade marks or infringement of other IPRs. The concept of "unfair competition" may even be in complete contradiction with competition law and policy. For example, parallel importers can be accused of "unfair competition" or "unfair trade" because they do not respect market segmentation obtained by application of trade mark rules, while this practice may, in effect, be anti-competitive and contravene competition law. In extreme cases, even, there have been complaints by cartel members that outsiders were competing "unfairly", while in fact the cartel itself was in clear breach of the competition law.

18. An attempt to show the interconnection between these different (sometimes contradictory) laws and concepts is made in chart 1. In any event, as discussed above, there is, at present, a growing consensus in all countries that effective competition policy cannot be conducted without adoption of specific competition law. The law entails the creation of a specialized Competition Authority, having the necessary powers to remedy anti-competitive restraints and to advise Government on possible anti-competitive effects of other laws.

Chart 1. The relationship between competion law and other laws and concepts

	Competition	Trade law	FDI	IPR	Consumer Protection	Unfair competition/ Unfair trade	Price regulation
Competition		Export cartel Protectionist or discriminatory application of competition legislation	Merger/acquisitions Abuse of DPMP Cartels of FDI RBPs by local firms	Prohibition of RBP in licensing procedure	Prohibition of unfair trade practices Obligatory display of prices	Discriminatory application of competition law	Price liberalization Prohibition of resale price maintenance (RPM)
Trade law	Anti-dumping Subsidies		Export incentives, subsidies to FDI	Counterfeit trade	Safety regulations Health protection Phytosanitary rules	Anti-dumping action Countervailing duties Use of trade marks to prohibit parallel imports VERs	Administrative pricing of imports
Investment (FDI)	FDI incentives, such as tax holidays or granting of monopolies to FDI, can be anti-competitive	Local content requirements TRIMs		Registration of trade marks and other IPRs in favour of FDI			
IPR	Use of trade marks to ban parallel imports	Trade mark import restraints Restraints on trade anciliary to licensing agreement	Licenses and royalties in parent/Subsidiary operations		Trade mark indication of origin	Trade marks Copyrights Industrial designs Patents Rules of origin	Resale price maintenance and price regulation resulting from IPR

Chart 1. The relationship between competition law and other laws and concepts (continued)

	Competition	Trade law	FDI	IPR	Consumer Protection	Unfair competition/ Unfair trade	Price regulation
Consumer protection law	Misleading advertising Misrepresentations	Health and safety standards	Prohibition of imports of goods banned in parent country	Rules of origin Standards		Misleading advertising Weights and measures (metrology)	Prohibition of hoarding and other price manipulations
Unfair trade or unfair competition laws	Provisions sometimes found in competition law	Anti-dumping Subsidies Rules of origin	Predatory pricing of inputs and technology in parent subsidiary relations	Counterfeit trade	Hoarding Predation Pyramid-selling Bait-selling Misleading representation and advertising		Export subsidies Dumping
Price regulation	In case of urgency where competition law is not efficient (e.g. brutal hike of prices of essential goods such as petrol)	Subsidized exports	May either subsidize (if low price of inputs) or hinder FDI (if high price of inputs)	Compulsory licensing Administrative regulation of license conditions, royalties and sales	Low prices and subsidizing of primary necessities	Subsidized exports	

Chapter II

DIFFERENT APPROACHES TO COMPETITION LEGISLATION

A. Existing laws and laws in preparation

19. At present, all developed (OECD) countries have competition legislation. Moreover, the European Union and the European Economic Area countries apply competition regulations to trade transactions among member States. In addition, in recent years, a growing number of developing countries and countries in transition have also adopted similar statutes. The following developing countries or territories had or were preparing laws in 1995:

Latin America and Caribbean	Africa	Asia and Pacific
Argentina	Kenya	China
Brazil	Gabon	Fiji
Bolivia*	Ghana*	India
Chile	Morocco*	Indonesia*
Colombia	South Africa	Malaysia*
Costa Rica	Tunisia	Pakistan
El Salvador*	Zambia	Philippines*
Guatemala*	Zimbabwe*	Republic of Korea
Jamaica		Sri Lanka
Panama		Thailand
Paraguay*		Taiwan Province of China
Peru		
Trinidad and Tobago*		
Venezuela		

* Competition law in preparation.

Among countries in transition, Poland, Hungary, the Czech Republic, Lithuania, the Russian Federation and many other members of the CIS, including Ukraine, Belarus and Georgia, have adopted competition (anti-monopoly) legislation. A compendium of these laws, with related commentaries, is regularly updated in UNCTAD's Handbook of RBP Laws. Issues already published are indicated below:

Competition laws of the following countries	Handbook document No.
France, Republic of Korea	TD/B/RBP/42
Denmark, Poland, Spain, USA	TD/RBP/CONF.3/5
Chile, Portugal, Sri Lanka	TD/B/RBP/49
Canada, Sweden	TD/B/RBP/58
Germany, Finland	TD/B/RBP/71
Pakistan	TD/B/RBP/33
Kenya	TD/B/RBP/58/Add.1
Brazil, Norway	TD/B/RBP/82
United Kingdom	TD/B/RBP/87
Belgium	TD/B/RBP/87/Add.1
Italy, Jamaica, Venezuela	TD/B/RBP/94
Lithuania, Mexico, Slovakia, Zambia	TD/RBP/CONF.4/3

B. Structural versus behavioural control

20. Most laws deal with enterprise behaviour by combating horizontal RBPs (cartels) and fighting abuses of dominant positions of market power in vertical RBPs. Structural action is mainly concerned with merger control, the aim being to avoid creating dominant firms or monopolies as a result of concentration of market power. Some laws, however (such as in the United States), have the possibility of ordering divestiture of dominant firms in order to change the structure of the markets.

C. Terminology and structure of basic competition law

21. As described in much more detail the commentary to the Model Law or Laws (see UNCTAD document TD/B/RBP/81/Rev.4), there are many different types of competition laws and systems. Even the titles of the laws differ considerably. The first competition law was the Combines Act of 1889 in Canada, followed by the United States-anti-trust laws (Sherman Act in 1890). In the United Kingdom and countries following the United Kingdom model, after 1947 restrictive trade practices laws and monopolies and restrictive trade practices (MRTP) laws were enacted. In the 1970s, OECD, then UNCTAD, adopted the terminology of restrictive business practices (RBPs) law, which was more recently changed to competition law. Countries in transition have called their laws anti-monopoly laws. However, irrespective of their different names, the basic structure of all competition laws is broadly the same, and usually covers the following aspects:

Structure of basic competition law:

Objectives

Definitions

Scope of application

Exemptions and exceptions

Prohibited practices: horizontal and vertical

Merger control

The Competition Authority

Sanctions

Appeal procedure

22. Although certain converging trends have been discernable in recent years, it should be made clear at the outset that competition law is "tailor-made" for each country, depending on a variety of factors, including the judicial system and the customs, business culture, market size, level of development, etc., of that country. The main differences are described below.

(i) Objectives

23. Objectives have been multiple in time and include optimal allocation of resources, avoiding undue concentration of economic power in a few hands, fighting inflation, and protecting consumer interests, as well as broad, loosely defined concepts involving the notion of public interest. The most recent trend is essentially that of defending and promoting competition itself, it being understood that by so doing the law will promote efficient allocation of resources in the economy, resulting in the best possible choice of quality, the lowest prices, 2/ and adequate supplies for consumers.

Objectives of competition law

1. To promote competition, which ensures efficiency and optimal allocation of resources for the benefit of consumers, users of intermediate products, and the economy as a whole

2. To encourage innovation

3. To control concentration of economic power

4. To ensure a fair distribution of income

5. To combat inflation

6. To ensure full employment

7. To defend "public interest"

Trends in modern laws

1. To promote competition

2. To maximize economic efficiency

(ii) Definitions

24. Restrictive business practices are often not defined by legislation, but rather specific RBPs are usually listed in a non-exhaustive manner. In general, the term enterprises is defined to include all firms, TNCs, their branches, subsidiaries, small and medium-sized enterprises (SMEs), and State-owned enterprises (SOEs) engaged in commerce or business. Monopolies are usually defined as a single supplier in a given market. However, some legislations use the term monopoly or monopolization in a sense similar to that of "dominant firm".

25. Definitions of dominant firm, or enterprise enjoying a dominant position of market power, vary from country to country, but the basic idea is that a dominant firm is one which is able to control the "relevant market" in which it operates. This is achieved when the dominant firm is able to fix its prices and conditions of sales without being challenged by its competitors.

Other suppliers are present in the market, but they simply adjust to the pricing decisions of the dominant firm. The latter is a price leader. Some laws contain the concept of "joint dominance", where a dominant position may be held when a firm, by itself, or together with a few others, is in a position to control the market. A detailed description of procedures used by most competition authorities in defining the relevant market and determining whether a firm has a dominant position in the market is to be found in chapter III, paragraphs 55-57, of this note.

26. It should be noted, however, that simply being a dominant firm is not in itself a breach of most competition laws. What most competition laws aim at is to prevent dominant firms taking advantage of their market strength to abuse their dominant position of market power (DPMP) by using restrictive business practices. (This will be further analysed in the context of vertical RBPs.)

27. Because of the danger that dominant firms (or monopolies) might restrain competition, competition laws usually prohibit dominant positions of market power or monopoly-creating mergers, acquisitions, or joint ventures. (This will be further discussed below in the context of merger control.)

(iii) Scope of application

28. As indicated above, all enterprises engaged in business, whether private, public or other, are usually covered by modern competition law (subject to exemptions; see below).

29. The law covers all transactions in goods and services. It also covers private persons such as those engaged in the liberal professions. (For example, in some countries "ethical codes" among doctors and lawyers prohibiting advertisement are now banned as being anti-competitive.) But collective bargaining and trade unions are always exempted.

30. Most competition laws cover the national territory and do not extend outside national boundaries. A few laws, those of the United States in particular, have extraterritorial application. Although this is relatively limited by considerations of "comity" (i.e. considering the sovereign interests of other nations with which the extraterritorial application of jurisdiction might conflict), the extraterritorial application of laws often results in problems with other countries defending their national sovereignty.

(iv) Exemptions and exceptions 3/

31. As a result of deregulation, the number of specific sector regulations creating exemptions and exceptions from competition law has tended to decrease. However, until recently very numerous exemptions and exceptions to competition law existed, and some are still applied:

- Sovereign acts of State are not covered by competition laws. In other words, the Government can always pass a law having anti-competitive consequences. It might also sign a treaty, or

international agreement having anti-competitive effects (see provision B.9 of the Set of Principles and Rules, which exempts such international agreements from the prohibitions in the Set). Recent trends, however, have increased the advocacy functions of competition authorities, which, under modern competition laws, are given the task of advising the Government on competition matters to avoid the enactment of laws with unnecessarily anti-competitive side-effects.

- Traditionally, labour markets (trade unions), collective wage bargaining and setting of conditions of employment are not covered by competition laws.

- Regulated industries and sectors of the economy which are still excluded from the scope of competition legislation today, in spite of deregulation, include in many cases agriculture, oil extraction, mining, and "natural" monopolies such as postal services and utilities. In some countries, the defence industry is also exempted. However, deregulation has seriously reduced the preserve of some service sectors, such as banking, insurance, shipping, air transport, etc., in numerous countries.

- Utilities and "natural" monopolies. It was long believed that competition was not possible in certain sectors such as the postal service, electric power, gas, water distribution, city bus transportation, etc., which were "natural" monopolies. However, as a result of technological change, the extent of "natural" monopolies has also started to be reduced, for example in the case of cable TV, mobile telephones, etc. In those countries most advanced in introducing competition in regulated sectors, such as the United Kingdom for example, monopolies are reduced to the extent possible, including by means of privatization and divestiture of services which are not considered "natural" monopolies. (For example, gas distribution is now performed by competing firms, the only service remaining a "natural" monopoly being the grid-network.) And the Competition Authority or the regulatory agency is requested to keep an eye on the operations of remaining monopolies to ensure that their dominant power does not spill over from the monopoly sector into sectors where competition should prevail. In some countries, special regulatory agencies (such as OFTEL, OFFAS, etc., in the United Kingdom) have been established to monitor the activity of privatized utilities and to ensure that they operate according to the rules of competition.

- Another type of exemption concerns small and medium-sized enterprises (SMEs), often involving the application of a threshold (usually 5 per cent of the relevant market) below which the possible anti-competitive effects are considered to be insignificant. Such firms may be allowed to cooperate among themselves (horizontal or vertical agreements) if by so doing they

increase their countervailing market power relative to large firms (in Germany, for example) and hence increase competition in a given market.

- Given the gigantic research and development investments necessary to develop certain new products, R & D joint ventures are also subject to exemptions in many countries (such as the United States and the European Union).

- Specific distribution agreements (motor cars, perfumes) obtain "block exemptions" in the EU, provided they meet certain conditions and are notified to the Commission.

- Export cartels and "joint ventures for export" deemed not to have effects on the domestic market are often exempted by law (United States, United Kingdom, "pure export cartels" in Germany) after being notified to the Competition Authority. In many countries the competition law simply does not deal with export cartels when they have no effects on the domestic market, and hence such cartels do not require notification, because the law only applies to the domestic market.

- Rationalization as well as crisis cartels and recession cartels are authorized by law in some countries (Germany, Japan) and are expected to be disbanded when the cause for such authorization is no longer valid.

D. Prohibited practices: horizontal and vertical practices

32. It is important to note that the types of prohibition vary from country to country. The strongest type of prohibition is the *per se* approach applied in particular in the United States with respect to horizontal RBPs, such as price-fixing, market allocation and collusive tendering or bid-rigging. Horizontal agreements can never be authorized, and when discovered are automatically challenged. The *per se* approach has tended to be used by many countries with respect to collusive tendering or bid-rigging.

33. However, apart from bid-rigging, a relatively more lenient approach can be found with respect to horizontal RBPs in other countries, such as the EU, which applies a prohibition in principle approach. In other words, article 85 of the Treaty of Rome prohibits price-fixing and market allocation, but immediately envisages the possibility of granting an exemption (art. 85 (3)) if the benefits of the restraint outweigh the damage to competition and if consumers obtain a substantive share of the benefits (in terms of improved distribution channels, better quality and enhanced technical progress, for example). Other laws still have more lenient approaches. For example, in some countries cartels are only required to be notified and registered, and upon a complaint, only abuses found to be contrary to loosely defined "public interest" are subject to remedy action. After inquiry, the recommendations of the Competition Authority can be accepted (or rejected) by the Minister, and

as a result, the practices in question may be prohibited by the Minister. It is then only in case of breach of such a prohibition that fines may be imposed by the Courts.

34. Still weaker concepts exist which do not require notification, but upon inquiry into an abuse, the Competition Authority may recommend to the respective government authority (the Minister) that the restraint be prohibited.

35. As national competition laws are amended from time to time, the tendency has been to amend weak types of legislation and to adopt stricter approaches similar to those of the EU rules or United States anti-trust laws.

36. Vertical agreements are usually treated more leniently than horizontal agreements and collusive tendering, for example in the United States where, except for resale price maintenance, which is prohibited outright, the "rule-of-reason" applies to all other types of vertical RBPs, which have to be judged on a case-by-case basis.

37. Resale price maintenance is prohibited in most countries, while views differ with respect to "recommended prices", which are prohibited in some, authorized in others. However some sectors, such as publications and pharmaceuticals, are often exempted. In most countries, vertical practices other than resale price maintenance are only prohibited if imposed by monopolies or by dominant firms.

E. Merger control

38. As mergers, acquisitions and joint ventures can result in undue concentration of market power (creation of dominant firms, or of monopoly), they are usually closely scrutinized by competition authorities.

39. In many countries, merger control is subject to separate legislation. Some countries, although having competition laws, do not have merger control. The trend, however, is to include merger control as part and parcel of competition law.

40. In order to avoid an unnecessary burden on the business community and the Competition Authority, pre-merger notification is usually required for firms larger in size than a prescribed threshold. Some control authorities have the power to prohibit mergers when they are deemed to create a dominant position of market power and also, in some countries (but on rare occasions), to order divestiture of mergers which took place before the authority could take action.

F. Consumer protection

41. Many competition laws contain specific provisions which are usually found in separate consumer protection legislation. While, in some countries, specific consumer protection law is controlled by the same authority as that entrusted with monitoring implementation of the competition act, in others, the competition law contains a chapter devoted to consumer protection issues.

42. Specific consumer protection provisions, often entitled "unfair trade practices", include prohibition of hoarding, deceptive claims or misrepresentations, and misleading advertising, the obligation to label prices in shops (to increase price transparency and hence competition) and prohibition of particular marketing techniques such as bait selling 4/ and pyramid selling. 5/

G. The Competition Authority

43. All competition laws usually encompass the establishment of an administrative authority to monitor implementation of the law. The authority can be located in a ministry, usually the Ministry of Commerce, Trade and Industry, or the Ministry of Finance, Economics, or Justice.

44. In some countries, in addition to the Competition Authority which is part of a Ministry, there is also an independent competition commission or council, which has distinct functions. The Ministry may refer specific cases for investigation by the commission or the council (e.g. references to the Monopolies and Mergers Commission in the United Kingdom, or the Competition Council (Conseil de la Concurrence) in France). One trend is that competition authorities are increasingly established as bodies having a certain independence from the government, in order to ensure that their pro-competition advocacy function to the ministries and government agencies is not distorted by considerations other than competition. A new trend in some countries has been to create a "superintendency" dealing with both competition law and other legislation, such as consumer protection legislation, intellectual property rules, misleading advertising legislation, etc.

H. Sanctions

45. Certain countries, like the United States, apply criminal law to "hard-core" RBPs such as price-fixing and bid-rigging. Individuals can have jail sentences and fines imposed upon them by the courts. Germany and the European Commission, however, apply only administrative sanctions in the form of fines on enterprises only. The amounts, however, can be substantial - as high as 10 per cent of the turnover of the firm. Some countries apply administrative fines to firms and to their administrators, if found guilty of serious contraventions of competition law. In the United Kingdom, the law does not impose sanctions; it is only if the defendant is found to be in breach of a court order to cease and desist that fines and even prison sentences can be imposed.

46. In any event, in order to be credible, the competition authority must have the powers to impose credible sanctions.

I. Damages

47. Many laws provide for compensation for damages resulting from breaches of competition law. The United States has a particular system of treble damages whereby the injured party may recover three times the amount of the losses resulting from an RBP.

J. Class actions

48. Some laws provide for the possibility of anti-trust action for a "class" or number of people each of whom has lost relatively small amounts of money as a result of a breach of competition law, for example taxi customers who have had to pay more as a result of an unlawful price-fixing arrangement.

K. Appeal procedures

49. All competition laws provide for appeal procedures of one sort or another to a special trade court or tribunal, to higher courts or to the Supreme Court.

Chapter III

BASIC PROCEDURES FOR INVESTIGATING RBPs OR MERGERS

50. In the same way as competition laws differ from country to country but have important "common ground", similar common ground can also be found in the basic procedures of an investigation. While the systems of investigation leading to a decision and sanctions may vary, 6/ the basic technicalities of an investigation are very similar. The various steps of an investigation are described below.

A. Initiating an investigation

(i) Sources of information

51. An investigation may be initiated as a result of a complaint from a consumer, a businessman, a government authority or the Competition Authority itself. Some laws limit the possibility of complaints to associations of consumers or businesses, excluding individual action.

52. The Authority may initiate an investigation on its own count as a result of its own research into price rises or irregularities denounced in the press. Often, restrictive business practices are denounced by former employees who have lost their jobs and who want to take revenge on their former employer. In the United States and, to a certain extent in the EU, the firm which denounces an illegal agreement in which it has taken part may be granted total or partial immunity or a lowering of the level of sanctions. In the case of merger control, the law often requires prior notification of mergers, with the Competition Authority being given a time limit for its reaction (no more than one month usually).

(ii) Preliminary assessment of the case

53. The Competition Authority usually completes a memorandum of investigation, in which it indicates the product, the alleged illegal practice, the section of the law which might be infringed, the names of the parties involved, and the geographic area covered by the alleged malpractice. Before contacting the firms, the Competition Authority will try to complete its information from public sources (press, available data) and might keep the issue secret until surprise dawn raids are made if evidence needs to be found.

54. As a result of a preliminary assessment of the case, the Authority may decide to drop the case or to pursue further its investigations if it finds there is legitimate cause for concern.

(iii) Analysis of the market

55. In order to analyse the market, the Competition Authority will have to clearly define the relevant market, both in terms of geographical area and the product or service concerned. The definition of dominant position of market power is based on the concept of the relevant market, which is the market of reasonably substitutable goods or services, i.e. "the area of effective

competition" (United States Supreme Court). The major tests used to define the relevant market, and by extension whether a firm is dominant in that market, are as follows:

- First, competition authorities consider to what extent the product in question can be substituted by another, if its price rises (e.g. would beer drinkers switch to lemonade or soft drinks?);

- Second, they analyse the scope for substitution; for this, they have to consider consumer tastes and preferences (demand substitution);

- Third, they consider the degree of transparency of the market (i.e. price-knowledge and price-sensitivity of consumers); are consumers well-educated, competition-minded?

- Fourth, the relevant market might be limited to a region or a remote area if, for example, communications are bad and costs of transportation prohibitive; it might be the domestic market if high protective walls exist at the border; or, the relevant market might be the world market in the case of an open economy and a product which can be imported at low cost;

- And fifth, they need to define the product or service to be considered, e.g. all motor cars or cars in a specific price range.

The relevant market test

1. Possibility of substitution

2. Scope of substitution, according to consumer tastes

3. Degree of transparency, knowledge about prices, and response of consumers

4. Relevant geographical area

5. Definition of the product or service to be considered

56. Once the relevant market is defined, the Competition Authority can then analyse it to see if there is dominant position of market power. First, it will be necessary to determine the degree of concentration of the relevant market. Is there a monopoly? Do two firms control more than x per cent, or three firms more than y per cent? (This depends on the competition law.)

57. Laws often provide for a presumption of dominance when a firm has a market-share of more than 25 or 33 per cent. The second test is to analyse the effects on competition of firms having large market-shares. Is there price parallelism? Do smaller firms "follow the leader" in setting prices, or do they compete vigorously? If competition is stifled, then competition authorities should consider the third test, i.e. entry conditions into the relevant market. Is there potential or actual competition? Is it made difficult, or impossible, for outsiders to enter the relevant market (by government ordinance, for example, in regulated markets or because of quotas or prohibitive tariffs on imports? Is exit made impossible by subsidies? Finally, the characteristics of the market will have to be examined: is there a dynamic (high-growth) or stable (mature) market? What is the relative size (and hence importance) of the market, and is it a government-regulated market?

Tests to determine the existence of DPMP

1. **Market share**
2. **Effects on competition**
3. **Entry/exit conditions**
4. **Characteristics of the market:**
   - **Dynamic or stable market**
   - **Relative size in the market**
   - **Government regulations**

B. The search for evidence

(i) Search of premises

58. In order to maximize the chances of finding evidence, in countries where the law authorizes search of premises (such as France, Germany and the United Kingdom), surprise dawn raids may be launched by the Competition

Authority. Normally, a warrant will have to be delivered by a judge to authorize such a search. Before a search, investigators should be well prepared in terms of knowing what they are looking for and where they are most likely to find proof (e.g. computer specialists may be needed, as the information required may be stored in computers and very difficult to find).

(ii) Questionnaires to firms

59. Letters and official requests for information can be sent to the firms involved.

(iii) Announcements in newspapers

60. Announcements can be placed in newspapers inviting evidence from third parties, customers or businesses that have suffered from the alleged practices, or that may have information to provide.

(iv) Hearings

61. Hearings can be held involving representatives of firms, accompanied by their lawyers. Often hearings are held separately, to avoid concerted action by defendants.

(v) Interim measures

62. Depending on the procedure used, an inquiry may last several months or even years in some cases. Some laws provide for the adoption of interim measures, usually in the form of a cease and desist order, pending the results of the investigation. It is often the case, however, that once an inquiry has been initiated, the defendants automatically abandon the alleged practices in order to avoid possible harsh sanctions.

C. Decisions and remedies

63. Depending on the results of the inquiry, the Competition Authority (or the court) will make a decision. This might be either a straightforward prohibition, or a conditional authorization, for example authorization of a merger provided one of the firms divests itself of certain interests or gives an undertaking to refrain from specific restrictive practices. The investigation may also conclude that the practices in question were not anti-competitive and are therefore authorized. In other cases, the law may provide for specific block exemptions, which may be granted. However, this does not usually require a full investigation. Block exemptions are usually adopted to reduce the burden of work on the Competition Authority and to reduce delays and backlogs of the Competition Authority. Provided specific conditions are met (e.g. specific types of restraints, relative size of the market covered by the agreement, etc.), the practices may be automatically granted a "block exemption".

64. Sanctions may be imposed by the Competition Authority in countries where the law gives it the power to impose fines, otherwise it is the courts that may impose pecuniary sanctions on firms and in some cases on individuals responsible for breaking the law. Some laws also provide for prison

sentences. In any event, the sanction has to be serious enough for the law to be credible. In countries with high inflation, for example, the maximum pecuniary sanctions fixed by the law may fast become unconvincing as a threat.

65. Damages are also provided for in modern competition laws. Consumers and third parties which have suffered from a condemned practice may sue the defendants for damages.

Notes

1/ The Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices was adopted by the General Assembly in resolution 35/63 of 5 December 1980 (TD/RBP/CONF.10/Rev.1).

2/ It should be noted that, as regulated prices are scrapped in most countries, they are replaced by competition legislation, which is a more refined way of controlling the competitive formation of prices rather than fixing prices administratively. After the Second World War, countries such as Sweden, Norway and France had administered prices. These were then gradually replaced by modern competition legislation.

3/ An exemption is usually broad in scope (a whole sector, such as mining or agriculture), while exceptions are granted to particular firms in specific cases.

4/ Bait selling (prix d'appel) is a practice whereby consumers are attracted by very important discounts on one product which is only available in limited supply.

5/ Pyramid selling involves advantages (rebates) for those who manage to sell the product to others who sell to others and so on.

6/ For example, in the United Kingdom, three main bodies deal with an investigation: the Office of Fair Trading (OFT), the Monopolies and Mergers Commission (MMC) and the Department of Trade and Industry (DTI), plus the Restrictive Trade Practices Court. This system of multiple "checks and balances" involves a first screening by the OFT, which may then refer a case to the MMC for investigation, the recommendation of which may lead to an order by the DTI Minister if he accepts the recommendation of the MMC. An order may be obtained from court. Unless an order is subsequently breached by the enterprises in question and they are found in "contempt of court", there are no fines applied when the Minister accepts the recommendations of the MMC. In Germany, on the other hand, the Federal Cartel Office has quasi-judicial powers to initiate an inquiry, to proceed with investigations and make a decision which may include fines imposed on the defendants, who may appeal to courts on procedural matters only. Exceptionally, the Minister of Economics may reverse a merger prohibition. In the United States, the Justice Department may initiate a case, but will have to challenge the defendants in court. Sanctions are imposed by the courts (both fines and jail sentences). The Federal Trade Commission (FTC), on the other hand, has administrative powers, but sanctions are imposed by the courts.

Annex 1

CHECKLIST OF ARGUMENTS OFTEN PUT FORWARD AGAINST THE ADOPTION OF COMPETITION LEGISLATION

- There is a need for critical size, critical mass or economies of scale for enterprises to become competitive on the international market.

- It is important to avoid "more bureaucracy" in times of deregulation and "less government".

- Developing countries do not need a competition policy. Only sophisticated advanced economies can handle such a complicated procedure.

- Adopting competition law will scare away badly needed FDI.

- Open markets will suffice to bring in import competition.

- Competition laws give excessive powers to single corruptible individuals. There is a need for careful checks and balances.

- The complexity of proper competition analysis makes it impossible for developing countries to implement effective competition law and policy.

- Competition policy will wipe out domestic industry in the face of giant foreign firms which benefit from market power, advanced technology and "the deep pockets" of their parent firm.

Annex 2

DIFFICULTIES AND LIMITATIONS OFTEN ENCOUNTERED BY COMPETITION AUTHORITIES

1. The Minister concerned may overturn a decision for "public interest" reasons, such as fear of increasing unemployment, or as a result of pressure from lobbies and activist groups.

2. A change of government may change the fate of the Competition Authority: some governments may be "politically" interested in competition law in connection with the breaking-up of monopolies or concentration of wealth in a few hands, while others might, on the contrary, be interested in defending or creating "national champions", or may be unwilling to apply competition laws that might hinder vested interests.

3. Other administrative bodies (regulatory agencies) might have functions that overlap with that of the Competition Authority (e.g. regulatory bodies created to control privatized utilities might have competition responsibilities which should rest with the Competition Authority). When decisions are difficult to make, the regulatory body might still require the Competition Authority to study the matter, otherwise it might make the wrong (anti-competitive) decision.

4. Lawmakers and other Ministries (Health, Trade, etc.) might adopt legislation without considering its anti-competitive side-effects, irrespective of the Competition Authority's advocacy functions.

5. Powerful businessmen might sometimes be closer to the powers of command (Minister) than the head of the Competition Authority. Ministers may accept excessive concessions to large foreign direct investors making employment (or other) promises. As a result, foreign firms might get subsidies, tax holidays, long-term import authorizations on concession terms, while domestic competitors are denied such advantages.

Budgetary constraints/limited means

6. Budget limitations might hamper the capacity of the Competition Authority to undertake required action. For example, one Competition Authority stated that it hesitated to use the media to publicize its functions for fear that they would receive too many complaints which they would certainly be unable to treat correctly, running the risk of losing credibility.

7. A Competition Authority may lack the financial resources to employ high-level staff, and it may have to rely on local police and judiciary who are not trained for competition rules.

8. A Competition Authority may lose its staff as a result of promotions or better employment opportunities in the private sector soon after they have received good training abroad.

Absence of reliable business statistics

9. There may be a lack of reliable data and statistics in developing countries, resulting in an inability to make a case correctly or to be able to determine market dominance, e.g. if the market share of a firm is unknown.

Lack of credibility of Competition Authority decisions

10. An inadequate level of fines may lend to lack of credibility of the Competition Authority.

11. The Competition Authority may be obliged to carry on with the staff of the previous price-regulating administration who do not understand the principles of competition and their new responsibilities.

12. The length of the investigation and the judiciary process, including appeals, often without intermediary measures, may reduce the impact of decisions of the Competition Authority.

Novelty of the subject for consumers

13. Competition principles are new for consumers used to relying on administrative pricing. The Competition Authority needs to educate consumers and create a "competition culture", that encourages consumers to "shop around" and compare prices, something they might not appreciate at all at first.